

PLACER UNIT

DECISION ON REMAND FROM THE COMMISSIONER  
CONDITIONALLY APPROVING AELLC'S APPLICATIONS AND APPEALS TO  
EXPAND THE PLACER UNIT AND TO AMEND ITS PLAN OF EXPLORATION

FINDINGS AND DECISION OF THE DIRECTOR  
DIVISION OF OIL AND GAS  
UNDER DELEGATION OF AUTHORITY FROM THE COMMISSIONER  
DEPARTMENT OF NATURAL RESOURCES  
STATE OF ALASKA

NOVEMBER 13, 2014

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## **I. INTRODUCTION**

This is the decision on remand of the Alaska Department of Natural Resources (DNR), Division of Oil and Gas (Division), conditionally granting the requests ASRC Exploration, LLC (AELLC) made in its August 17, 2012 application to expand the Placer Unit (PLU) area and to amend the PLU Plan of Exploration (POE) to change the location and to extend the deadline for drilling a new unit well as modified by AELLC's subsequent appeals and response to DNR's request for an appropriate cure for unit default.

## **II. FACTS**

On September 8, 2011, the Division Director approved AELLC's unit formation application. The PLU was formed out of portions of four state leases, ADLs 391023, 391024, 391027, and 391028, totaling 1,480 acres in size. The portions of these leases not included in the unit (hereinafter Expansion Area) were severed from the portions of the leases included in the unit, given new lease numbers, and granted a two-year extension of the primary term to January 31, 2014. The Division's decision to approve the PLU relied in part on AELLC's commitment to either drill and log a new unit exploratory well in the unit area or to re-enter and test the existing Placer #1 well by June 30, 2013.

Shortly after the Division approved the PLU, AELLC submitted an application to the Division to expand the PLU to include the Expansion Area, to allow AELLC to meet the well commitment by drilling in the Expansion Area, and to extend the drilling deadline. On January 14, 2013, the Division Director issued a decision denying the August 17, 2012 application because it was inappropriate to expand the unit before AELLC met the commitments upon which unit approval was based.

AELLC failed to either drill a new well or re-enter and test the Placer # 1 well by June 30, 2013. By letter dated July 25, 2013, DNR notified AELLC that the PLU was in default for failure to comply with the terms of the initial POE requiring the aforementioned well work. The notice of default gave AELLC until June 30, 2014 to either drill and log a unit exploratory well or re-enter and test the Placer #1 well.

On October 9, 2013, the Division denied a new POE submitted by AELLC because it proposed to drill an exploration well outside of the PLU. On September 12, 2013, AELLC and Brooks Range Petroleum Company (BRPC) met with the Division and presented a confidential slide deck which described four well options to delineate the PLU. All of the options proposed that AELLC enter into a farm-out agreement with BRPC so that BRPC could drill the required well and that the well be drilled in the Expansion Area.

AELLC then sent the DNR Commissioner a letter dated September 18, 2013 again stating AELLC's intention to farm-out the right to drill to BRPC, again requesting that DNR include the Expansion Area in the unit and extend the drilling deadline, and asking the Commissioner to issue a decision on the still pending appeal from AELLC's August 17, 2012 application to expand the unit and defer the drilling commitment.

On September 24, 2013, the DNR Commissioner remanded AELLC's PLU appeal from the Division's denial of AELLC's August 17, 2012 application to expand the unit and to defer the drilling commitment back to Division. The Commissioner requested the Division to approve inclusion of the Expansion Area in the unit and to extend the drilling deadline on certain conditions including but not limited to: (1) the required well must be drilled by 2014, (2) no modification of the original five-year unit term provided for by 11 AAC 83.336, (3) AELLC must provide a performance bond in an amount to be set by the Division to ensure that the drilling requirement is met, and (4) AELLC must provide DNR with a copy of the farm-out agreement between AELLC and BRPC.

On November 4, 2013, the Division issued a decision implementing the Commissioner's instructions on remand. This decision required, in part, that AELLC provide DNR with a copy of the AELLC-BRPC farm-out agreement and the performance bond by December 15, 2013. The Division extended that deadline to December 20, 2013 and then to January 10, 2014. But AELLC neither provided DNR a copy of an executed farm-out agreement or any performance bonds.

On January 13, 2014, the Division notified the DNR Commissioner by letter that AELLC had not met the conditions set out in the Commissioner's remand decision, that the unit was not expanded, and that the PLU remained in default and had no currently approved POE. AELLC had until June 30, 2014 to drill the required well.

AELLC failed to cure the unit default by drilling a well within the approved unit by June 30, 2014. On July 18, 2014, the Commissioner sent AELLC a notice of opportunity to be heard on the appropriate remedy for unit default.

On August 7, 2014, AELLC made a supplemental filing with DNR on the pending appeals and on remedy for default. AELLC requested a hearing before the DNR Commissioner during the week of August 11, 2014, on its pending appeals and the Notice. By agreement, the hearing was conducted by the DNR Commissioner on August 18, 2014. At the hearing, AELLC insisted that DNR expand the PLU and authorize AELLC to drill the exploratory well in the Expansion Area. Material presented by AELLC at the hearing indicated that an exploratory well would be drilled by May 31, 2016. After the hearing, AELLC submitted a 2014 POE and annual report to the Division. The 2014 POE was denied on September 17, 2014, and AELLC appealed that decision.

All of AELLC's appeals and response to the notice of opportunity to be heard make the same requests: include the Expansion Area in the PLU, authorize the required well to be drilled in the Expansion Area, and extend the deadline for drilling the well.

On October 23, 2014, the DNR Commissioner again remanded AELLC's pending appeals to the Division Director. The remand decision stated in part:

The unit expansion and POE extension are approved on the following conditions:

- AELLC must drill an exploratory well in the PLU Expansion Area at the location it proposed to DNR and also specified herein by May 31, 2016.

- The well needs to be drilled in the area shown on page 4 of attachment 1 of the AELLC's November 22, 2013 appeal filing and labeled "Proposed Placer #3" and slide 9 of AELLC's presentation slide of August 18, 2014. Both of these CONFIDENTIAL documents are attached to this decision, and will be kept in DNR records as confidential unless there is subsequent authorization to disclose them from AELLC, a court, or another authority.
- AELLC must provide a \$2.5 million dollar performance bond securing its commitment to drill a new exploratory well by May 31, 2016, to compensate the State for its economic loss if the well is not drilled.
- The Director is requested to issue a decision implementing the unit expansion, the drilling extension, and the conditions set forth herein as soon as reasonably possible.
- The Director is requested to include in his decision, a schedule of reasonable deadlines to accomplish key steps necessary to allow the well to be drilled by May 31, 2016. The deadlines shall include, but are not limited to, timelines to secure a drilling rig for the winter/spring 2016 target drilling season and timely application for and receipt of an Oil Discharge Prevention and Contingency Plan.
- AELLC must submit a new POE incorporating the conditions set forth herein and the conditions set forth in the Director's decision requested here.

The 11 AAC 83.336 five-year deadline of September 8, 2016 for unit expansion is not reset by this order and the Director shall not reset it in his decision. The PLU expires September 8, 2016 unless the conditions of 11 AAC 83.336 are met.

### III. RELEVANT STATUTORY, REGULATORY, AND UNIT AGREEMENT PROVISIONS

The statutory standard for unitization is whether it would be necessary and advisable in the public interest:

To conserve the natural resources of all or a part of an oil or gas pool, field, or like area, the lessees and their representatives may unite with each other, or jointly or separately with others, in collectively adopting or operating under a cooperative or a unit plan of development or operation of the pool, field, or like area, or a part of it, when determined and certified by the commissioner to be necessary or advisable in the public interest. (Emphasis added).

DNR has set forth unitization decision criteria in regulation that retain the public interest as the primary criterion:

**11 AAC 83.303. Criteria.** (a) The commissioner will approve a proposed unit agreement for state oil and gas leases if he makes a written finding that the agreement is necessary or advisable to protect the public interest considering the provisions of AS 38.05.180(p) and this section. The commissioner will approve a proposed unit agreement upon a written finding that it will

- (1) promote conservation of all natural resources, including all or part of an oil or gas pool, field, or like area;
  - (2) promote the prevention of economic and physical waste; and
  - (3) provide for the protection of all parties of interest, including the state.
- (b) In evaluating the above criteria, the commissioner will consider
- (1) the environmental costs and benefits of unitized exploration or development;
  - (2) the geological and engineering characteristics of the potential hydrocarbon accumulation or reservoir proposed for unitization;
  - (3) prior exploration activities in the proposed unit area;
  - (4) the applicant's plans for exploration or development of the unit area;
  - (5) the economic costs and benefits to the state; and
  - (6) any other relevant factors, including measures to mitigate impacts identified above, the commissioner determines necessary or advisable to protect the public interest.
- (c) The commissioner will consider the criteria in (a) and (b) of this section when evaluating each requested authorization or approval under 11 AAC 83.301 - 11 AAC 83.395, including
- (1) an approval of a unit agreement;
  - (2) an extension or amendment of a unit agreement;
  - (3) a plan or amendment of a plan of exploration, development or operations;
  - (4) a participating area; or
  - (5) a proposed or revised production or cost allocation formula.

A unit terminates five years after formation unless certain conditions are met.

#### **11 AAC 83.336. Effective date and term of unit agreement**

- (a) A unit agreement becomes effective upon approval by the commissioner and automatically terminates five years from the effective date unless

(1) a unit well in the unit area has been certified as capable of producing hydrocarbons in paying quantities, in which case the unit agreement will remain in effect for so long as hydrocarbons are produced in paying quantities from the unit area, or for so long as hydrocarbons can be produced in paying quantities and unit operations are being conducted in accordance with an approved unit plan of exploration or development, or, should production cease, for so long after that as diligent operations are in progress to restore production and then so long after that as unitized substances are produced in paying quantities; or

(2) exploration operations have been conducted in accordance with an approved unit plan of exploration, and the commissioner, after issuing written notice under 11 AAC 83.311, issues a written decision extending the unit term in which he states the basis for his decision, considering the provisions of 11 AAC 83.303; no single extension will exceed five years.

(b) If a suspension of unit operations or production on all or part of the unit area has been ordered or approved under federal, state, or local law, or, if the commissioner determines that the unit operator has been prevented, despite good-faith efforts, from complying with any express or implied promise, term, condition, or covenant of the unit agreement, or from conducting exploration, development, production, transportation, or marketing operations on or from the unitized area by reason of force majeure, the unit operator's obligation to comply with the provision will be held in abeyance, but not voided, and the commissioner will extend the term of the unit agreement for a period of time equal to the time lost under the unit term due to the suspension or prevention by force majeure. . . .

### **Placer Unit Agreement**

Article 13 of the unit agreement addresses unit expansion. It states in relevant part:

13.1. The Unit Operator, at its own election may, or at the direction of the Commissioner shall, apply to expand the Unit Area to include any additional lands determined to overlie a Reservoir that is at least partially within the Unit Area, or to include any additional lands that facilitate production. . . .

## **IV. DECISION**

The PLU is expanded to include ADLs 391910, 391911, 391912, and 391913 (Expansion Leases). Below is a schedule for AELLC to adhere to upon approval of the unit expansion and POE extension.

1. By January 15, 2015, AELLC must provide a \$2.5 million performance bond securing its commitment to drill a new exploratory well by the date stated below.



2. By December 31, 2014, AELLC must submit a new POE incorporating the conditions set forth in this decision and the Commissioner's October 23, 2014 Remand Decision.
3. AELLC must meet the deadlines, set forth below, necessary for the exploratory well to be drilled on time.
  - Submit to the Division a fully-executed agreement securing a drilling rig for the winter/spring 2016 drilling season on or before June 30, 2015.
  - Submit for approval a Placer Unit Plan of Operations to the Division to drill the proposed Placer #3 well on or before August 30, 2015.
  - Provide evidence of approval from the Department of Environmental Conservation for the Placer Unit's Oil Discharge Prevention and Contingency Plan on or before December 1, 2015.
4. On or before May 31, 2016, AELLC must drill an exploratory well in the PLU Expansion Area.
  - The exploratory well needs to be drilled in the Expansion Area as shown on page 4 of attachment 1 of the AELLC's November 22, 2013 appeal filing and labeled "Proposed Placer #3" and slide 9 of AELLC's presentation slide of August 18, 2014. The exploratory well shall be drilled through the base of the Kuparuk River Formation as correlated in the Placer #1 well.
  - If the well is not drilled through the base of the Kuparuk River Formation as correlated in the Placer #1 well, logged and tested, or plugged and abandoned by May 31, 2016, the bond will be retained by DNR. If the well is drilled through the base of the Kuparuk River Formation as correlated in the Placer #1 well, logged and tested, or plugged and abandoned by May 31, 2016, DNR will return the bond to AELLC.

The above conditions are necessary to protect the State's interest given AELLC's prior failure to comply with work commitments. The DNR Commissioner's October 23, 2014 decision to remand AELLC's pending PLU appeals to the Division, considers the 11 AAC 83.303 decision criteria, and that decision found that bringing the Expansion Area into the PLU and modifying the drilling area and deadlines was in the public interest because these actions promote conservation of natural resources, promote the prevention of waste, and protect the parties' interests, but only if AELLC secures performance with a \$2.5 million dollar bond and the Division sets deadlines to ensure the new well will be drilled in a timely manner. The Division incorporates by reference the Commissioner's consideration of the 11 AAC 83.303 decision criteria herein.

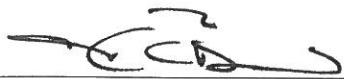
This decision becomes effective upon the Division's receipt of a performance bond deposit in favor of the DNR which DNR may retain if AELLC fails to drill the required well by May 31, 2016. This decision does not reset the five-year unit term from its original formation date of September 8, 2011. The PLU, including the Expansion Area, expires September 8, 2016 unless the conditions of 11 AAC 83.336 are met.



The leases approved for inclusion in the expanded PLU are summarized below.

ADL	Acres	State Royalty Interest %	Lease Effective Date	Working Interest Owners and Percentages	Lease Expiration Date	Legal Description
391910	480	16.66667	2/1/2007	AELLC 100%	1/31/2014	T. 11N., R. 7 E., Umiat Meridian, Alaska Sec 4: NE1/4NE1/4, 40 ac Sec 9: E1/2NE1/4, SW1/4NE1/4, S1/23, 440 ac
391911	1909	16.66667	2/1/2007	AELLC 100%	1/31/2014	T. 11N., R. 7E., Umiat Meridian, Alaska Sec 5: W1/2SW1/4, N1/2NW1/4, SW1/4NW1/4, 200 ac Sec 6: All, 593 ac Sec 7: All, 596 ac Sec 8: SW1/4NE1/4, S1/2, NW1/4, 520 ac
391912	2480	16.66667	2/1/2007	AELLC 100%	1/31/2014	T. 12 N., R. 7 E., Tract A, Umiat Meridian, Alaska Sec 27: All, 640 ac Sec 28: All, 640 ac Sec 33: E1/2, N1/2SW1/4, NW1/4, 560 ac Sec 34: All, 640 ac
391913	2419	16.66667	2/1/2007	AELLC 100%	1/31/2014	T. 12 N., R. 7 E., Tract A, Umiat Meridian, Alaska Sec 29: All, 640 ac Sec 30: All, 588 ac Sec 31: All, 591 ac Sec 32: N1/2, N1/2SE1/4, SW1/4SE1/4, SW1/4, 600 ac
<b>TOTAL</b>	7288					

A person affected by this decision may appeal it, in accordance with 11 AAC 02.010 through 11 AAC 02.900. Any appeal must be received within 20 calendar days after the date of "issuance" of this decision, as defined in 11 AAC 02.040(c) and (d), and may be mailed or delivered to Joe Balash, Commissioner, DNR, 550 W. 7<sup>th</sup> Avenue, Suite 1400, Anchorage, Alaska 99501; faxed to (907) 269-8918, or sent by electronic mail to [dnr.appeals@alaska.gov](mailto:dnr.appeals@alaska.gov). This decision takes effect immediately. An eligible person must first appeal this decision in accordance with 11 AAC 02.010 through 11 AAC 02.900 before appealing this decision to Superior Court. A copy of 11 AAC 02.010 through 11 AAC 02.900 may be obtained from any regional information office of the Department of Natural Resources.

  
W.C. Barron  
Director  
Division of Oil and Gas

  
Date